

***The U.S. Treasury Department  
Summary Response to GAO Recommendations***

*September 21, 2009*

The Treasury Department (Treasury) welcomes the recommendations on the Troubled Asset Relief Program (TARP) made by the GAO in its July 2009 report: *Treasury Actions Needed to Make the Home Affordable Modification Program More Transparent and Accountable*.

Treasury works closely with the GAO on a daily basis regarding TARP programs, including the Home Affordable Modification Program (HAMP). Communication with the GAO includes responding to specific inquiries and organizing comprehensive briefings on the progress of HAMP with senior Treasury staff. Treasury keeps the GAO apprised of its progress on implementing recommendations, as well as on developments with current and proposed programs and policies under the Emergency Economic Stabilization Act of 2008 (EESA).

This report first identifies each GAO recommendation issued in its July 2009 report on HAMP and then provides a summary of Treasury's actions to address the specific recommendation. As described below, Treasury's Office of Financial Stability (OFS) continues to make tremendous progress in administering the HAMP program.

**GAO Recommendation 1:**

*Consider methods of (1) monitoring whether borrowers with total household debt of over 55 percent of their income who have been told that they must obtain HUD-approved housing counseling do so, and (2) assessing how this counseling affects the performance of modified loans to see if the requirement is having its intended effect of limiting re-defaults.*

Summary of Treasury's Actions in Response to this GAO Recommendation

Treasury believes that housing counseling is beneficial for high debt-to-income borrowers. Therefore, Treasury requires such borrowers to certify that they will obtain counseling. Borrowers participating in HAMP are provided a list of local HUD-approved housing counseling agencies from which to select an appropriate counselor.

Counseling may have the benefit of helping to reduce re-defaults among borrowers with high total debt burdens. Treasury is exploring options for monitoring what proportion of borrowers is, in fact, obtaining counseling. Servicers have expressed concerns, however, about the potential difficulty and burden of communication with counseling agencies to certify that borrowers had received counseling. Treasury is first and foremost committed to preventing foreclosures and does not plan to deny modifications to borrowers who successfully complete the trial period and meet the other requirements for a HAMP modification, even if it is not feasible to confirm that they obtained counseling.

**GAO Recommendation 2:**

*Reevaluate the basis and design of the HPDP program to ensure that HAMP funds are being used efficiently to maximize the number of borrowers who are helped under HAMP and to maximize overall benefits of utilizing taxpayer dollars.*

**Summary of Treasury's Actions in Response to this GAO Recommendation**

In response to both GAO recommendations and as a result of internal analysis, Treasury made two fundamental changes in the Home Price Decline Protection (HPDP) program prior to its introduction. Both of these changes will improve the targeting of the subsidy. First, the size of HPDP incentive payments is based on the size of the unpaid principal balance (UPB) of the mortgage, as opposed to the property's value, as was originally described in early program documents. Mortgages with higher UPB stand to lose more value in the case of default and, therefore, are provided with larger HPDP incentive payments. Second, HPDP incentive payments are scaled according to the mark-to-market loan-to-value market ratio (LTV): mortgages with higher LTVs will receive higher HPDP incentive payments.

These changes improve the targeting of HPDP payments and will help ensure a greater number of borrowers in areas with rapid and recent home price declines have the opportunity to stay in their homes. These changes will also help to stabilize housing prices in impacted areas.

Treasury believes that making HPDP incentives available only for loans that would not otherwise pass the NPV test would potentially result in a reduced number of modifications for otherwise eligible borrowers. Under an approach where the HPDP subsidy is set so that loans just pass the NPV test, servicers would have an incentive to select the highest discount rates and most pessimistic re-default rate in order to maximize the HPDP subsidy per loan modified. However, these assumptions could result in fewer loans passing overall. Therefore, this approach would either require a reworking of the NPV process to eliminate all servicer choice, or risk resulting in a reduced number of modifications as servicers select the highest discount rates and most pessimistic re-default rates in order to maximize HPDP payments.

**GAO Recommendation 3:**

*Institute a system to routinely review and update key assumptions and projections about the housing market and the behavior of mortgage holders, borrowers, and servicers that underlie Treasury's projection of the number of borrowers whose loans are likely to be modified under HAMP and revise the projection as necessary in order to assess the program's effectiveness and structure.*

**Summary of Treasury's Actions in Response to this GAO Recommendation**

The scope and impact of the HAMP program is monitored through regular and comprehensive data collection from HAMP participating servicers. This data collection covers a broad array of economic and demographic characteristics of the specific subset of mortgage borrowers who are participating in HAMP. In addition to HAMP-specific

data collection, Treasury actively monitors the nation's housing markets through evaluation of aggregate statistics, which include sales, prices, housing starts, delinquencies and foreclosures, as well as the analysis of loan level data. Treasury actively coordinates with other agencies to monitor the nation's housing markets.

Treasury makes HAMP-specific market data publicly available by publishing monthly reports detailing servicer-by-servicer performance, the number of trial modifications started, the number of trial period plan offers extended to borrowers, and the number of requests for financial information sent to borrowers on its *MakingHomeAffordable.gov* website.

Because the HAMP program is the first of its kind, in designing projections, Treasury's interagency team, which included representatives from Treasury, the Federal Reserve, HUD, Fannie Mae, Freddie Mac, FHFA, and other agencies, relied on existing program data that mimicked certain features of HAMP to generate key assumptions about the behavior of program participants.

Treasury continues to gather data on modifications as it becomes available, such as data from the FDIC/IndyMac modification program and early phases of HAMP. In addition, Treasury recently engaged the FDIC to explore the possibility of transitioning from OCC/OTS data to FDIC/IndyMac data by the end of the year for certain components of the projection. Treasury will continue to use the best available information to improve and build upon the assumptions underlying projections about mortgage market behavior.

Treasury also continues to review and refine the NPV model. Treasury's inter-agency NPV modeling team, which includes representatives from the agencies mentioned above, has assembled a list of model improvements to be incorporated into the next version of the NPV model. The forthcoming NPV model will include improvements to underlying assumptions and the use of additional data sources to estimate key components, such as the default and prepayment models.

#### **GAO Recommendation 4:**

*Place a high priority on fully staffing vacant positions in HPO—including filling the position of Chief of Homeownership Preservation with a permanent placement—and evaluate HPO's staffing levels and competencies to determine whether they are sufficient and appropriate to effectively fulfill its HAMP governance responsibilities.*

#### Summary of Treasury's Actions in Response to this GAO Recommendation

The approach to hiring within HPO has been to hire HPO's directors first and then hire the staff below each director. Currently, HPO has a staff projection of 31 full time equivalents (FTE) for fiscal year 2009; at present, HPO has 23 full time staff and one detailee, with a projection of five hires by September 30, 2009.

Treasury continues to hire highly qualified individuals to administer HAMP. HPO is making excellent progress in staffing vacant positions and in hiring a permanent Chief.

Treasury will soon conduct its first quarterly review to evaluate the number of staff and their competencies.

**GAO Recommendation 5:**

*Expediently finalize a comprehensive system of internal control over HAMP, including policies, procedures, and guidance for program activities, to ensure that the interests of both the government and taxpayer are protected and that the program objectives and requirements are being met once loan modifications and incentive payments begin.*

Summary of Treasury's Actions in Response to this GAO Recommendation

Treasury has a comprehensive system of internal controls over HAMP. Evidence of Treasury's internal controls, including testing and implementation, has been provided to GAO. Treasury continues to refine its internal control environment through close interaction with its financial agents Fannie Mae and Freddie Mac.

Treasury has developed and implemented policies, procedures, and guidance over the HAMP program. Starting with the inception of HAMP, Treasury has publicly issued directives to guide program participants, which include borrowers, servicers, investors and financial agents. The six directives are available on Treasury's administrative website for HAMP: *HMPadmin.com*. As new programs are developed or revised, including HPDP and Second Lien programs, additional directives containing policies and procedures will be issued as necessary to coincide with program implementation.

Treasury is also working with Fannie Mae and Freddie Mac, two of its financial agents, to assess the design and refine the internal controls implemented within their operations, including regular meetings exclusively on internal controls. The continuous implementation of new program components will require Treasury, Fannie Mae, and Freddie Mac to continue to work together to build out and refine internal control processes critical to HAMP's ongoing success.

**GAO Recommendation 6:**

*Expediently develop a means of systematically assessing servicers' capacity to meet program requirements during program admission so that Treasury can understand and address any risks associated with individual servicers' abilities to fulfill program requirements, including those related to data reporting and collection.*

Summary of Treasury's Actions in Response to this GAO Recommendation

Treasury has worked with its financial agent, Freddie Mac, to develop a means of assessing servicers' capacity to meet program requirements. There are various components of the compliance program which address servicers' ability. An on-site review is conducted and includes walkthroughs of processes including borrower solicitation, eligibility, data collection and reporting and a review of supporting evidence of process effectiveness. By September 30<sup>th</sup>, the first round of on-site reviews for

servicers representing 88 percent of the total cap allocation will have been completed. Beginning in October, servicer reviews will take place within 30 to 45 days of signing a servicer participation agreement with Treasury. Reviews of all servicers who have elected to code the NPV model into their own system, rather than use the portal application have also been completed. New requests to code the NPV model in a servicer's proprietary application or changes to existing models must be tested and approved prior to implementation. Treasury does not believe these reviews need to be linked to the admission process because, upon admission, a servicer becomes contractually obligated to review a borrower for eligibility for HAMP before beginning any foreclosure actions.